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In the Supreme Court of the United States

OCTOBER TERM, 1998

DAIMLERCHRYSLER CORPORATION,

PETITIONER,

V.

KOLOSSO AUTO SALES, INC.,

RESPONDENT.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF THE ASSOCIATION OF INTERNATIONAL AUTOMOBILE MANUFACTURERS, INC., GENERAL MOTORS CORPORATION AND FORD MOTOR COMPANY AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF THE *AMICI CURIAE*[1]

The Association of International Automobile Manufacturers, Inc. ("AIAM") is a trade association representing domestic subsidiaries of international automobile manufacturers doing business in the United States and abroad.[2] One of the AIAM's most important functions has been to represent the interests of its members in litigation pending before the courts of the United States.

The AIAM's members have a vital interest in protecting the franchise agreements negotiated between automobile manufacturers and their dealers from unwarranted impairment by the states. As discussed in more detail below, forty-nine states regulate franchise relationships between automobile manufacturers and dealers. Accordingly, the AIAM has sought to advance the interests of its members by filing amicus briefs in numerous cases involving state motor vehicle franchise statutes, as well as other issues of substantial importance to automobile manufacturers. For example, the AIAM has recently filed *amicus* briefs before this Court in *State Oil Co. v. Khan,* 522 U.S. 3 (1997) and in *Kumho Tire Co., Ltd., v. Carmichael,* 131 F.3d 1433 (11th Cir. 1997), *cert. granted,* 118 S. Ct. 2339 (U.S. June 22, 1998) (No. 97-1709).

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[1] Pursuant to Rule 37.6 of the Rules of this Court, *amici* state that no counsel for a party has authored this brief, in whole or in part, and that no person or entity, other than *amici,* their members, or their counsel, has made a monetary contribution to the preparation or submission of this brief. Letters have been filed with the Clerk of the Court confirming that all parties have consented to the submission of this brief.

[2] The Association's members include: American Honda Motor Co., Inc.; American Suzuki Motor Corp.; BMW of North America, Inc.; Fiat Auto U.S.A., Inc.; Ferrari North America, Inc.; Hyundai Motor America; Isuzu Motors America, Inc.; Kia Motors America, Inc.; Land Rover North America, Inc.; Mazda North American Operations; Mercedes-Benz of North America, Inc.; Mitsubishi Motor Sales of America, Inc.; Nissan North America, Inc.; Porsche Cars North America, Inc.; Rolls-Royce Motor Cars, Inc.; Subaru of America, Inc.; Toyota Motor Sales, U.S.A., Inc.; Volkswagen of America, Inc.; and Volvo Group North America, Inc. The Association also represents various manufacturers of tires and other original equipment with production facilities in the United States and abroad.

General Motors Corporation ("GM") and Ford Motor Company ("Ford") are the world's largest and second largest vehicle manufacturers, respectively. Like the AIAM's members, GM and Ford have a vital interest in protecting their agreements with dealers from unwarranted impairment by the states.

In the decision below, the Seventh Circuit held that a retroactive amendment to the Wisconsin Motor Vehicle Dealers Law, Wis. Stat. § 218.01, did not constitute a "substantial impairment" of the franchise contract between petitioner Chrysler Corporation and respondent Kolosso Auto Sales, Inc. and, therefore, did not violate the Contract Clause of the United States Constitution. In so doing, the Seventh Circuit became the first circuit to uphold the constitutionality of such retroactive franchise legislation.

The Seventh Circuit's interpretation of the Contract Clause conflicts with prior decisions of this Court and other courts of appeals, and jeopardizes the enforceability of material terms in tens of thousands of contracts between automobile manufacturers and their dealers. This Court should grant review to resolve this important conflict now in order to forestall further disruption of the constitutionally protected contractual rights of automobile manufacturers. Accordingly, *amici* respectfully urge this Court to grant the petition for a writ of certiorari and reverse the decision of the circuit court.

SUMMARY OF ARGUMENT

In the decision below, the Seventh Circuit held that the State of Wisconsin did not violate the Contract Clause when it abrogated manufacturers' existing contractual rights to control the location of their dealerships. The court of appeals held that the retroactive regulation of contractual terms governing franchise *relocation* was "foreseeable" at the time petitioner executed its contract—and therefore unprotected by the Contract Clause—because the Wisconsin Motor Vehicle Dealers Law, Wis. Stat. § 218.01, regulated the *termination* of automobile franchise agreements at that time.

As petitioner demonstrates, the Seventh Circuit's opinion conflicts with controlling Supreme Court authority requiring that state laws which impair contracts serve a valid public purpose, *see* Petition at pp. 11-15, and creates a split among the circuits regarding the constitutionality of retroactive franchise legislation, *id.* at pp. 15-20. In becoming the first court of appeals to uphold such legislation, the Seventh Circuit has unsettled the contractual expectations of an industry where most, if not all, franchise agreements designate a specific franchise location and require manufacturer approval of any relocation. These relocation clauses are of central importance to the parties' bargain.

This Court's precedents firmly establish that the Seventh Circuit's foreseeability analysis unreasonably circumscribes the important protections afforded by the Contract Clause. Even though the State of Wisconsin had never before regulated contract provisions governing the relocation of automobile franchises, the court of appeals held that such regulation could be foreseen—as a matter of law—based upon the State's prior regulation of contract termination. Under this Court's precedents, however, the relevant inquiry is whether the specific contractual term at issue—not some other contract term—was subject to regulation when the contract was executed. *See, e.g., Veix v. Sixth Ward Building & Loan Ass'n,* 310 U.S. 32, 38 (1940) (holding that a party who purchases an enterprise "already regulated *in the particular to which he now objects*" purchased subject to further legislation "upon the same topic") (emphasis added). The Seventh Circuit abandoned this principle in favor of an open-ended "foreseeability" standard that undermines the very purpose of the Contract Clause, which is "to encourage trade and credit by promoting confidence in the stability of contractual obligations." *United States Trust Co. v. New Jersey,* 431 U.S. 1, 15 (1977) (citing *Home Building & Loan Ass'n v. Blaisdell,* 290 U.S. 398, 427-28 (1934)).

Taken to its logical conclusion, the Seventh Circuit's analysis would effectively eliminate Contract Clause protections in the

automobile industry and other regulated franchise industries. Once a state has chosen to regulate franchise termination, virtually every other provision of the franchise agreement could be subject to retroactive impairment by the state on the theory that any plausible regulation is foreseeable as a matter of law. Yet there is no substantial justification for retroactively altering the contract rights of manufacturers—rights which often determine whether a manufacturer will succeed or fail in a local market. In light of the fact that forty-nine states regulate automobile franchise relationships, and forty-eight of those states currently regulate the termination of such franchises, the Seventh Circuit's decision will engender widespread uncertainty regarding the enforceability of franchise agreements and encourage other jurisdictions to follow Wisconsin's lead in the adoption of unconstitutional regulations abrogating critical contractual terms. *Amici* respectfully urge this Court to grant the petition for a writ of certiorari and reverse the decision of the Seventh Circuit.

ARGUMENT

I. THE SEVENTH CIRCUIT'S HOLDING CONFLICTS WITH THIS COURT'S PRECEDENTS CONCERNING THE EFFECT OF PRIOR REGULATION ON THE SCOPE OF THE PROTECTION AFFORDED BY THE CONTRACT CLAUSE

The Seventh Circuit's focus on the purported "foreseeability" of the Wisconsin statute at issue has its roots in two opinions of this Court: *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400 (1983) and *Veix v. Sixth Ward Building & Loan Ass'n*, 310 U.S. 32 (1940). *See* Pet. App. at 6a. In each of those cases, this Court rejected the Contract Clause challenges, relying in part on the fact that the specific contract terms at issue were subject to pre-existing state regulation. *See Kansas Power & Light*, 459 U.S. at 411; *Veix*, 310 U.S. at 38. This Court concluded that the "reasonable expectations" of the parties were

not impaired under these circumstances. *Kansas Power & Light,* 459 U.S. at 416; *see also Veix,* 310 U.S. at 38.

In determining whether a challenged regulation has impaired the reasonable expectations of the contracting parties, this Court has invariably focused on the question of whether the specific contractual provision at issue—as opposed to the general subject matter of the agreement—was regulated at the time of contracting. *See, e.g., Kansas Power & Light,* 459 U.S. at 413-16 (holding that state statute regulating natural gas prices did not "substantially impair" contract for purchase of natural gas, where such prices had been extensively regulated by the state and federal government for many years, and where the contract at issue specifically provided for changes in price depending upon regulatory changes); *see also Veix,* 310 U.S. at 38 (holding that changes in New Jersey statute regulating withdrawals from building and loan associations did not violate Contract Clause where such withdrawal rights were regulated at the time of plaintiff's purchase). As this Court held in *Veix,* "[w]hen [plaintiff] purchased into an enterprise already regulated *in the particular to which he now objects,* he purchased subject to further legislation upon the same topic." *Veix,* 310 U.S. at 38 (emphasis added).

The Seventh Circuit did not adhere to these holdings. The court acknowledged that the State of Wisconsin had never before regulated the relocation of automobile franchises.[3] *See* Pet. App. at 7a. It nevertheless held that the retroactive regulation of franchise relocation did not constitute a "substantial impairment" under the Contract Clause because the Wisconsin statute already regulated termination—a completely separate aspect of the relationship. Pet. App. at 6a-11a. Under *Veix* and *Kansas Power &*

[3] As the Seventh Circuit noted, prior to the 1993 amendment, the statute's only reference to relocation was a provision permitting a dealer to complain if another dealer relocated into the complaining dealer's relevant market area. *See* Pet. App. at 7a. That provision, of course, did not restrict a manufacturer's right to deny a dealer's request to relocate. *Id.*

Light, however, contracting parties were only found to have assumed the risk that regulations governing a specific "topic" of their contract could be changed by the state. Armed with the knowledge that certain terms of a contractual relationship have been subjected to regulation—and, hence, to regulatory change—the contracting parties could take the risk of such changes into account in negotiating their agreement. But parties are not required to guess whether and how the state might choose to regulate an entirely different aspect of their relationship at some unspecified point in the future.

The Seventh Circuit's "foreseeability" analysis requires precisely such speculation. Indeed, as the Seventh Circuit itself recognized, the "evolution" from the existing regulation of termination to the provision regulating relocation was merely "plausible" at the time of the contract. Pet. App. at 7a. As such, it is unreasonable to presume that the contracting parties could have taken such an "evolution" into account when negotiating their agreement. By shifting the focus of the "foreseeability" (or "reasonable expectations") inquiry away from the specific contractual term at issue—in this case, franchise relocation—and toward the general subject matter of the contract, the Seventh Circuit fundamentally altered the governing standard established in *Veix* and in *Kansas Power & Light*. In order to restore the rule established by this Court more than a half century ago, and to ensure that the legitimate economic interests of contracting parties are afforded the protection mandated by the Constitution, this Court should grant the petition for a writ of certiorari and reverse the Seventh Circuit's decision.

II. THE SEVENTH CIRCUIT'S OPINION WILL ENGENDER WIDESPREAD UNCERTAINTY REGARDING THE ENFORCEABILITY OF FRANCHISE CONTRACT TERMS, AND ENCOURAGE THE ADOPTION OF UNCONSTITUTIONAL REGULATIONS IN OTHER STATES

The Seventh Circuit's failure to adhere to this Court's controlling precedents has obviously impaired hundreds of contracts in the

State of Wisconsin. The effects of the Seventh Circuit's decision will extend far beyond the Wisconsin borders, however. Virtually all automobile franchise agreements require dealers to operate from a specific location and facilities previously approved by the manufacturer, and foreclose relocations without the approval of the manufacturer. The reason for such provisions is manifest: the location of an automobile franchise is a critical factor to success in the marketplace. *See, e.g., Kaiser v. General Motors Corp.*, 396 F. Supp. 33, 40 (E.D. Pa. 1975) ("[T]he lower courts have uniformly sustained the reasonableness and legality of the franchise location clause in actions brought under the Automobile Dealers' Day in Court Act . . . ."); *see also Gus Machado Buick-GMC Truck, Inc. v. General Motors Corp.*, 623 So.2d 810, 813 (Fla. Dist. Ct. App. 1993) ("Location is certainly an important consideration in any type of franchise agreement . . . ."). In the wake of the Seventh Circuit's opinion, however, the enforceability of those provisions is now in doubt.

Nor are the effects of the Seventh Circuit's decision limited to the issue of relocation. In fact, the Seventh Circuit explicitly recognized that its reasoning applied to any contractual terms restricting a dealer's freedom of action:

> [T]he law's curtailment of the manufacturer's right of termination cast a cloud over *all* contractual clauses restricting a dealer's freedom of action, any one of which might be challenged in application as unfair, unreasonable, inequitable, unprovoked, or, in short, as not being based on good cause.

Pet. App. at 7a (emphasis in original).

Thus, according to the Seventh Circuit, if a manufacturer's right to terminate a franchise agreement is subject to regulation at the time of contracting, all of the other contractual rights for which the manufacturer has negotiated may be subject to retroactive nullification by the State. Not even the Wisconsin statute purported to go so far in eviscerating the contractual rights of

manufacturers. In the very provision cited by the Seventh Circuit, which prohibits manufacturers from terminating franchise agreements "unfairly, without due regard to the equities or without just provocation," the statute defines "just provocation" to include a "material breach" of the franchise agreement by the dealer. *See* Wis. Stat. § 218.01(3)(17). Notwithstanding the implicit protection for the manufacturer's contractual rights embodied in this provision, the Seventh Circuit held that such rights are subject to change, at any time, by retroactive statute.

The implications of the Seventh Circuit's reasoning are practically endless. At this time, forty-nine states regulate the relationships between automobile manufacturers and their dealers; all but one of those states specifically regulate the termination of such relationships. Under the circuit court's "foreseeability" analysis, the terms of every dealer agreement in those states—and in any other state that chooses to regulate franchise termination in the future—may be subject to retroactive change.

As a result, the contractual rights obtained by manufacturers are all at risk of abrogation by state legislatures that may be inclined to advance aggressively the economic welfare of in-state dealers at the expense of out-of-state manufacturers. Having bargained for certain warranty and other service obligations on the part of the dealer, for example, the manufacturer must live with the risk that the dealer will be relieved of such obligations, retroactively, by the state.

Under the Seventh Circuit's analysis, in other words, a party that agreed to a contractual obligation can simply appeal to the legislature for relief from that obligation. With such uncertainty regarding the enforceability of their contract rights, manufacturers will be unable to make even the most basic business decisions—such as pricing and distribution—in a rational fashion. That is precisely what the Contract Clause was designed to prevent. *See, e.g., United States Trust Co. v. New Jersey*, 431 U.S. 1, 15 (1977) (noting that Contract Clause was designed "to

encourage trade and credit by promoting confidence in the stability of contractual obligations").

If not corrected by this Court, the Seventh Circuit's decision in this case will cast doubt on the enforceability of automobile franchise agreements throughout the United States. In order to remove the uncertainty created by the Seventh Circuit's opinion, and to prevent the needless proliferation of unconstitutional regulation that undermines important contractual rights, this Court should grant review and reverse. *See, e.g., Allied Structural Steel Co. v. Spannaus,* 438 U.S. 234 (1978) (intervening to enforce limits on state power embodied in the Contracts Clause); *United States Trust Co. v. New Jersey,* 431 U.S. 1 (1977) (same).

CONCLUSION

For the reasons set forth, *amici* respectfully urge this Court to grant the petition for a writ of certiorari, and to reverse the decision of the court of appeals.

Respectfully submitted,

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